

Washington State Auditor's Office
Fraud Investigation Report

Lake Forest Park Water District
King County

Investigation Period
June 1, 2004 through January 31, 2011

Report No. 1009188

Issue Date
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WASHINGTON
TROY KELLEY
STATE AUDITOR



**Washington State Auditor
Troy Kelley**

February 19, 2013

Board of Commissioners
Lake Forest Park Water District
4029 N.E. 178th St.
Lake Forest Park, Washington 98155

Report on Governmental Fraud Investigation

Attached is the official report on a misappropriation at the Lake Forest Park Water District. On February 1, 2011, the District notified the State Auditor's Office of a potential loss of public funds. This notification was submitted to us under the provisions of state law (RCW 43.09.185).

This report contains the results of our investigation of the former Office Administrator's unallowable activities at the District from June 1, 2004 through January 31, 2011. The purpose of our investigation was to determine if a misappropriation had occurred.

Our investigation was performed under the authority of state law (RCW 43.09.260) and included procedures we considered necessary under the circumstances.

Questions about this report should be directed to Fraud Manager, Sarah Walker at (509) 454-3621.

**TROY KELLEY
STATE AUDITOR**

cc: Mr. Alan Kerley, General Manager

Fraud Investigation Report

**Lake Forest Park Water District
King County
June 1, 2004 through January 31, 2011**

INVESTIGATION SUMMARY

On February 1, 2011, the General Manager notified our Office regarding a potential loss of public funds as required by state law.

We initiated an investigation and determined the Office Administrator misappropriated District funds using multiple schemes, including payroll, credit cards and payments. Our investigation found misappropriations totaling \$352,641.43 and another \$21,400.48 in questionable payments between June 1, 2004, and January 31, 2011.

We determined the misappropriation was not detected in a timely manner because the Board of Commissioners did not provide adequate oversight and monitoring of the Office Administrator's activities to ensure the use of public funds was appropriate.

The Office Administrator began working at the District on June 7, 2004. The Commissioners placed her on paid administrative leave January 21, 2011. She was placed on unpaid administrative leave after January 28, 2011.

The District has filed a report with law enforcement. The United States Attorney's Office has also been notified of this case.

BACKGROUND

The District operated on annual budgets ranging from approximately \$372,000 in 2004 to \$1,320,000 in 2010. The District uses King County to process its payments. Between 2004 and 2010, the District's annual payments ranged from \$516,627 to \$1,445,181, including payroll. The range in payments from year to year is due to various capital projects. The District serves approximately 900 water customers and its annual utility revenues are approximately \$600,000.

During most of the years we reviewed, the District had two full time employees, two contracted staff and approximately three part-time or seasonal employees. The two full time employees were the Water Manager and the Office Administrator.

- The Water Manager was responsible for field operations, water distribution and compliance. He was responsible for purchases related to construction and maintenance. His title was changed to General Manager in January 2011.
- The Office Administrator was responsible for the administrative office functions, including cash receipting, payroll and payments.

Both employees reported directly to the three-member Board of Commissioners until the misappropriation was detected.

INVESTIGATION RESULTS

Our investigation focused on payroll and payments. The payments included District credit cards, cell phones, employee reimbursements and petty cash. Our investigation found misappropriations and questionable transactions as shown in the following table. The categories are described in detail below this chart.

Category	Misappropriation	Questionable
Payroll and benefits:		
Office Administrator		see note below
Child 1	\$ 36,024.31	\$ 91.85
Child 2	\$ 81,572.00	
Child 3	\$ 15,315.00	
Retirement benefits	\$ 3,619.90	
Payments:		
District general credit card	\$ 91,848.77	\$ 7,157.51
Office Administrator's personal credit card	\$ 20,389.48	\$ 2,336.17
District office supply store credit cards	\$ 11,112.26	\$ 4,129.24
Personal reimbursements	\$ 48,388.28	\$ 4,387.07
Mileage reimbursements	\$ 27,949.96	
Cell phone	\$ 1,008.83	
Petty cash	\$ 1,948.08	\$ 919.71
Other payments	\$ 13,464.56	\$ 2,378.93
Total	\$ 352,641.43	\$ 21,400.48

Payroll and benefits

Office Administrator

The Office Administrator's gross payroll payments totaled \$315,514.79 between July 2004 and February 2011. It appears no one reviewed her timesheets for reasonableness and accuracy. We reviewed her timesheets and found instances where correction tape was used to increase hours worked. We also found that she took several paid days off during the holiday season that were neither board-approved holidays nor approved annual leave. The lack of review and documentation means that we cannot determine how much of her time is truly work related or questionable.

During our review of payroll, we also found District payments to the Office Administrator's three children. We reviewed District records, including timesheets for each of the children and found:

Child 1

This child – an official part-time employee -- was paid for substantially more hours than were worked. Gross payroll payments in the name of this employee total \$56,351.91 between April 2005, when he was only 15 years old, and February 2011. Eight payments were made during 2005 and 2006, with the remainder made between February 2009 and February 2011.

In July 2009, he was hired to work part time by the current Water District Manager, who estimates that he worked an average of less than 20 hours a week. During our review, we found timesheets that were altered to increase the hours worked. For example, the timesheet for the week of November 23, 2009, was originally 5 hours and was altered to show 41.5 hours were worked. The increase in hours does not correspond with the Water District Manager's records of work performed for those weeks.

We reviewed each of the timesheets and found that some appeared to be completed by the child and others by the Office Administrator. We also found timesheets that appeared to be created by the Office Administrator and related payments were deposited into her personal account. Misappropriated payments for this child total \$36,024.31 and questionable payments total \$91.85.

Child 2

This child was officially an employee for a few days during spring 2007, when she was 15 years old, and several weeks during the summer of 2007. She was also rarely called on as temporary help. Gross payroll payments in the name of this child total \$84,791 between April 2007 and January 2011.

District Minutes for September 2007 state that she "will be leaving us to go back to school." We reviewed each of the timesheets and found that some appeared to be completed by the child and others by the Office Administrator. With only one exception, all payments were deposited into the Office Administrator's personal account. Also, we reviewed Child 2's personal bank records and found she was employed at other various establishments in 2009 and 2010. Misappropriated payments for this child total \$81,572.

Child 3

This person was never an official employee of the District. Gross payroll payments in the name of this child total \$15,315 between April 2010 and January 2011. In April 2010, this person was 15 years old. We reviewed all of the timesheets and found they appeared to be created by the Office Administrator. We also found all related payments were deposited into the Office Administrator's personal account. Misappropriated payments for this child total \$15,315.

The District had several security cameras, including one at the front door and in various offices. We reviewed the videos for the month of December 2010 which reaffirmed our conclusions.

We asked the Water Manager about the employment status of the Office Administrator's three children. He stated that her children would occasionally visit the District Office, but they usually did their homework or other things unrelated to office work. With the exception of the legitimate payroll mentioned above for children 1 and 2, the Manager was unaware that they were being paid as employees.

We reviewed the District budgets for 2004 through 2010 and found Child 1's payroll was only budgeted \$15,000 in 2009 and \$20,000 in 2010. For 2009, the budget amount corresponds to less than 20 hours a week. Neither of the other two children was included in any of the budgets reviewed although the other official employees were included.

Contributions paid to retirement plan

In 2009, the Office Administrator enrolled two of her children to the Washington State Department of Retirement Systems (DRS). Neither of them met the DRS eligibility requirements, nor did they meet the eligibility requirements set out in the Commissioner-approved District Employee Guide. The District made retirement contributions of \$3,619.90 for the two children.

Payments

District general credit card

The District maintained a general credit card account with two cards, one assigned to the District Water Manager and the other to the Office Administrator. Total District general credit card payments were approximately \$230,200 between July 2004 and January 2011. Charges on the Office Administrator's card totaled \$152,848.03 between November 2005 and January 2011. We reviewed the charges on the Office Administrator's card and found:

- **Items purchased for personal use**, such as home improvements, electronics, automotive and motorcycle related items (including vehicle sound systems), and purchases at department stores. We found fuel purchases even though the Office Administrator had requested reimbursement for mileage.
- **College tuition**. We also found several charges for college tuition for both the Office Administrator and her daughter. The continuing education section of the District Employee guide states, "Participation in programs requiring time off from work and payment of tuition or per diem expenses require prior approval from the Board... The employee requesting reimbursement must produce proof of successful completion and the class must be determined to be relevant to the position." We reviewed the District minutes and found no evidence of board approval, evaluation of relevance to the position or proof of successful completion.
- **Alterations to receipts** in the District payment support that were made to conceal the items purchased. For example, we reviewed support for a charge that appeared altered to make it unclear what was purchased. We contacted the vendor and found it was a dog kennel and pet supplies.
- **Questionable payments** for items that may or may not have been for District use.

Misappropriated general credit card payments total \$91,848.77 and questionable general credit card payments total \$7,157.51.

Office Administrator's personal credit card

We reviewed all District payments to the Office Administrator's personal credit card. Payments to her credit card vendor totaled \$29,639.49 between December 2008 and January 2011. We found:

- **Items purchased for personal use and paid for by the District**, such as clothing, video games, energy drinks, household items including furniture, electronics, groceries, wood laminate flooring and kitchen accessories.
- **Reimbursements by the District for items she purchased but subsequently returned.** For example, in March 2009, the Office Administrator purchased two photocopier drums that appeared to be for District use for \$321. She returned them the next day, resulting in a credit to her personal account, but the request for reimbursement and payment was made after the purchase and return.
- **Reimbursements for items that were never actually purchased.** For example, in July 2009, the Office Administrator was reimbursed \$585.32 for a purchase at an office supply store. The payment support indicated the Office Administrator used her personal credit card account for the purchase, however, review of her credit card records show there is no purchase for the reimbursed amount or vendor.
- **Alterations to receipts** in the District payment support that were made to conceal the items purchased.
- **Questionable payments** for items that may or may not have been for District use.

Misappropriated personal credit card payments total \$20,389.48 and questionable personal credit card payments total \$2,336.17.

District office supply store credit cards

The District had two office supply vendor credit cards. We reviewed District payments to both vendors, which totaled \$23,338.25 between October 2004 and January 2011. We found:

- **Items purchased for personal use**, such as gift cards, software, electronics, including computers that were not for District use.
- **Alterations to receipts** in the District payment support that were made to conceal the items purchased. For example, we reviewed support for two payments that showed the purchase of various office supplies like ink and paper. The office supply vendor confirmed that both purchases were actually for computers. Neither was for District use.
- **Questionable payments** for items that may or may not have been for District use.

Misappropriated office supply credit card payments total \$11,112.26 and questionable office supply credit card payments total \$4,129.24.

Personal reimbursements

The Office Administrator was paid \$97,015.91 in personal reimbursements between July 2004 and January 2011. We reviewed all of these payments and found:

- **Items purchased for personal use**, such as home improvement items, auto repair parts, motorcycle related items, purchases at department stores and electronics not for District use.
- **Reimbursements by the District for items she purchased but subsequently returned.** For example, in October 2007, the Office Administrator purchased \$1,630 in postage stamps and two days later returned all of the stamps resulting in a credit to her personal account. The request for reimbursement and payment was made after the purchase and return.
- **Reimbursement payments for items that were never actually purchased.** For example, in February 2008, the Office Administrator was reimbursed \$1,449.79 for a purchase at an office supply store. The payment support indicated the Office Administrator used her personal credit card account for the purchase, however, review of her credit card records show there is no purchase for the reimbursed amount or vendor.
- **Alterations to receipts** in the District payment support that were made to conceal the items purchased.
- **Questionable payments** for items that may or may not have been for District use.

Misappropriated reimbursement payments total \$48,388.28 and questionable reimbursement payments total \$4,387.07.

Mileage reimbursements

The District Employee Guide states, "Employees should not use their own personal vehicles in the course and scope of their employment, other than their normal commute to and from the workplace, unless approved in advance by the General Manager."

Included in the total personal reimbursement payments to the Office Administrator was mileage reimbursement of \$37,755.99 for more than 74,000 miles between July 2004 and January 2011. Support for most of the mileage payments included only the date and miles, without any indication of the business purpose or destination. We used current trends, average number of bank deposits and information from early 2005 to calculate an expectation of reasonable District mileage. Based on our estimate of 292 miles per month, we found the misappropriation to be \$27,949.96.

Cell phone

The District has two authorized cell phones, one for the Office Administrator and the other for the District Water Manager. The District paid at least \$6,700 to their cell provider between March 2007 and December 2010. We reviewed cell phone vendor payments and found that the District was paying for three lines. The extra line was

added in the Office Administrator's name in January 2008. Further, we found excessive use on the extra line, as follows:

Cell phone lines	Dates in service-end of review	Invoice amount	Minutes used	Texts	Kilobytes of Data use
Line 1--Office Administrator	03/2007 – 12/2010	\$5,390.35	4,411	425	923,011
Line 2--Office Administrator	01/2008 – 12/2010	\$1,008.83	20,679	317,848	1,020,797
Line 3--District Water Manager	11/2009 – 12/2010	\$314.15	4,615	16	0

Misappropriated cell phone payments total at least \$1,008.83. This is the amount paid for the unauthorized phone line.

Petty cash

The District has a petty cash account with an authorized \$500 balance. We reviewed payments totaling \$8,980.68 between July 2004 and December 2010. We found personal purchases, including payment for two of the Office Administrator's vehicle infractions. We also found payments for items that are questionable whether or not they were for District use. Misappropriated petty cash payments total \$1,948.08 and questionable payments total \$919.71.

Other payments

We reviewed a complete vendor listing that included District payments made between January 2004 and January 2011. We selected and reviewed an additional 28 payments totaling \$15,845.49 to a variety of vendors. We found misappropriation similar to the other areas reviewed, including three payments for gravel that were delivered to the Office Administrator's residence.

Misappropriated reimbursement payments total \$13,464.56 and questionable reimbursement payments total \$2,378.93.

Other information

In order to determine if any additional misappropriations occurred, we examined systems to which the former Office Administrator had access. We reviewed the utility system revenues and did not find additional misappropriation.

CONTROL WEAKNESSES

Internal controls at the District were not adequate to safeguard public resources. We found the following weaknesses allowed the misappropriation to occur:

- The Office Administrator was allowed to restrict access to District financial records. District staff told us that the Office Administrator kept a padlock on the filing cabinet where relevant records were stored, and that she held the only key. By controlling access to information on payroll, reimbursements, and similar documents, she was able to filter information available to the Water Manager and other staff who had first-hand knowledge of District activities.

- The District Water Manager and the Office Administrator both reported directly to the board, which meant that no one was in a position to provide direct daily supervision of the Office Administrator's activities.
- The Commissioners did not provide adequate oversight and monitoring of the Office Administrator's activities to ensure the use of public funds was appropriate.

RECOMMENDATION

We recommend the District strengthen internal controls over approval of payments to ensure adequate oversight and monitoring to safeguard public resources and compliance with District policies.

We recommend the District contact the Department of Retirement Systems regarding the results of this investigation, and to determine whether a refund of contributions is allowable.

We also recommend the District seek recovery of the misappropriated \$352,641.43 and related investigation costs of \$56,228 from the former Office Administrator and/or its insurance bonding company, as appropriate. Any compromise or settlement of this claim by the District must be approved in writing by the Attorney General and State Auditor as directed by state law (RCW 43.09.260). Assistant Attorney General Kathryn McLeod is the contact person for the Attorney General's Office and can be reached at (360) 586-7879 or kathrynm@atg.wa.gov. The contact for the State Auditor's Office is Jan M. Jutte, Deputy Director of State and Local Audit, who can be reached at (360) 902-0363 or jan.jutte@sao.wa.gov.

DISTRICT'S RESPONSE

Thank you for the opportunity to provide this response.

The District concurs that the former Office Administrator misappropriated public funds. The District would like to thank the State Auditor's Staff for their effort over the two year period of the investigation.

The District immediately strengthened its financial controls upon learning of the misappropriation. Please refer to State Audit Report No. 1009177.

The District would like to state that the misappropriation was found in its operating funds, as opposed to capital funds.

As a member of the Water and Sewer Risk Management Pool (WSRMP) the District will immediately seek recovery upon finalization of this report. The District is insured through an insurance policy providing employee fidelity coverage.

The District's Board and management remain committed to maintaining high quality water service at an affordable cost while protecting public funds.

STATE AUDITOR'S OFFICE REMARKS

We thank District officials and personnel for their assistance and cooperation during the investigation.



ABOUT THE STATE AUDITOR'S OFFICE

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Our mission is to work with our audit clients and citizens as an advocate for government accountability. As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

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